

**STATE OF ILLINOIS
ILLINOIS COMMERCE COMMISSION**

**ILLINOIS-AMERICAN WATER COMPANY,)
and THAMES WATER AQUA HOLDINGS,)
GmbH)**

Docket No. _____

**Joint Application For Approval Of Proposed)
Reorganization And Change In Control Of)
Illinois-American Water Company Pursuant To)
Section 7-204 Of The Illinois Public Utilities Act.)**

**DIRECT TESTIMONY

OF

MICHAEL CARMEDY**

DIRECT TESTIMONY OF MICHAEL CARMEDY

Q. PLEASE STATE YOUR NAME, BUSINESS ADDRESS AND TITLE

A. My name is Michael Carmedy. My business offices will be located at 1101 Laurel Oak Road, Mt. Laurel, NJ 08054. I am currently employed as the Senior Vice-President and Commercial Director of Thames Water Americas. I also serve as a Board member of Elizabethtown Water Company.

Q. PLEASE DESCRIBE YOUR EDUCATION AND EMPLOYMENT HISTORY.

A. From 1983 through 1986, I attended the University of Kent in Canterbury, England where I earned a Bachelors Degree in Accounting, with Honors. In 1990, I qualified as a Chartered Accountant. From 1986 to 1990, I worked as an Audit Trainee with Fraser and Russell, Chartered Accountants. From 1990 to 1991, I worked as an Audit Senior with Moores Rowland, Chartered Accountants. I joined Thames Water Plc ("Thames") in 1991 as a Senior Auditor in its Internal Audit Department. Throughout my career I have held a variety of increasingly responsible positions, including Supervising Auditor and Investigations and Special Audits Manager. In 1998, I moved to the position of Financial Controller, Thames Water U.L., Engineering. In this position, I became responsible for project management for major U.S. acquisitions. A more detailed curriculum vitae is attached as Exhibit 2.1.

Q. PLEASE DESCRIBE YOUR CURRENT EMPLOYMENT RESPONSIBILITIES.

A. As Senior Vice-President and Commercial Director for Thames Water Americas, my primary obligations are the supervision of project bids on behalf of Thames Water Americas, risk management, and the coordination of regulatory approvals related to the acquisition of American Water Works Company, Inc. ("American").

Q. PLEASE DESCRIBE THE PURPOSE OF YOUR TESTIMONY.

A. The purpose of my testimony is to provide the Illinois Commerce Commission (“Commission”) with information regarding the manner in which Illinois-American Water Company (“Illinois American”) will be managed and operated after the closing of the contemplated acquisition. The details of the acquisition are set forth in the Application and the Agreement referenced therein.¹ I will describe the terms of this acquisition from my perspective as a member of the Due Diligence Team representing Thames and RWE Aktiengesellschaft (“RWE”) with respect to the proposed transaction. As discussed herein and in the testimony of Illinois-American’s witness, Mr. Gloriod, the proposed transaction will have no adverse impact on Illinois-American’s operations, employees and customer rates. Additionally, the proposed transaction will have no adverse impact on the safety and reliability of the system. In fact, as discussed below, the transaction will offer many potential benefits to Illinois-American and its customers. More specifically, I will provide to the Commission information explaining how Thames will preserve and build upon the excellent reputation and record of Illinois-American and American after the transaction is completed. Illinois-American witness Mr. Gloriod will discuss how the transaction meets the requirements of Section 7-204(b) (220 ILCS 5/7-204(b)) of the Illinois Public Utilities Act (“PUA”).

Q. PLEASE DISCUSS THE TERMS OF THE AGREEMENT.

A. Pursuant to the terms of the Agreement and Plan of Merger (“Agreement”), dated September 16, 2001 by and among RWE, Thames Water Aqua Holdings GmbH (“Thames Holdings”), Apollo Acquisition Company (“Acquisition Corp.”), and

¹ A copy of the Agreement is included in the Appendix to Testimony as Exhibit A.

American, American will become a wholly-owned subsidiary of Thames Holdings which, in turn, is a wholly-owned subsidiary of RWE. Illinois-American will continue to be a subsidiary of American and will continue to exist as an Illinois public utility subject to the jurisdiction and regulation of the Commission under the PUA. The Agreement provides that each issued and outstanding share of Common Stock, par value \$1.25 per share, of American (“American Common Stock”) not owned by Thames Holdings, Acquisition Corp. or American, other than shares owned by any holder who invokes appraisal rights under Delaware law, shall be converted into the right to receive cash in consideration of \$46.00 per share. The current authorized capital stock of American consists of (i) 300 million shares of American Common Stock, (ii) 1,770,000 shares of Cumulative Preferred Stock, par value \$25.00 per share (the “Preferred Stock”), (iii) 750,000 shares of Cumulative Preference Stock, par value \$25.00 per share (the “Preference Stock”), and (iv) 3 million shares of Cumulative Preferential Stock, par value \$35.00 per share (the “Preferential Stock”). As of September 30, 2001, 99,971,542 shares of American Common Stock (excluding shares held by American as treasury shares), 101,777 shares of the Preferred Stock, 365,158 shares of the Preference Stock and no shares of the Preferential Stock were issued and outstanding. The Agreement requires American to redeem, prior to closing of the transaction, each outstanding share of the Preferred Stock at a redemption price of \$25.25 per share, plus full cumulative dividends thereon, and each outstanding share of the Preference Stock at a redemption price of \$25.00 per share, plus full cumulative dividends thereon. The Agreement also provides that, at the time of closing of the transaction, each share of American Common Stock owned by Thames Holdings, Acquisition Corp. or American shall automatically be

cancelled and cease to exist and no consideration shall be paid for such shares. Under the Agreement, RWE will provide Thames Holdings with sufficient funds to consummate the transaction. The Agreement will affect none of the outstanding debt owed and recorded as liabilities on the books of Illinois-American. Unless retired or redeemed in accordance with its terms, all of that outstanding debt will continue to be liabilities and obligations of Illinois-American. Likewise, none of Illinois-American's assets will be affected by the Agreement. That is to say, all of its assets will continue to be assets of Illinois-American.

Q. PLEASE BRIEFLY DESCRIBE THE RWE COMPANIES INVOLVED IN THE PROPOSED TRANSACTION.

A. RWE, Germany's fifth largest industrial group, is an international multi-utility service provider with core businesses in electricity, water, gas, waste management and utility-related services. RWE is active in more than 120 countries on six continents. Thames Holdings, a wholly-owned subsidiary of RWE, is the holding company for Thames. Thames operates the water division of Thames Holdings, bringing to Thames Holdings its extensive experience and expertise as the largest water and wastewater company in the United Kingdom and one of the largest water and wastewater companies in the world -- providing water-related services to over 43 million people throughout the United Kingdom, Australia, China, Indonesia, Malaysia, Puerto Rico, the United States, Turkey and other countries around the world. Copies of the corporate profiles of RWE and Thames are included in the Appendix to Testimony as Exhibits B and C, respectively.

89 **Q. PLEASE BRIEFLY DESCRIBE THE IMPACT ON ILLINOIS-AMERICAN'S**
90 **CORPORATE STRUCTURE.**

91 A. After closing of the acquisition described in the Agreement, Illinois-American will
92 continue to exist in the same corporate form as it does today and will continue to be a
93 subsidiary of American. It will remain a public utility subject to the jurisdiction and
94 regulation of the Commission under the PUA. A diagram of the transaction is included in
95 the Appendix to Testimony as Exhibit G. As a result of the transaction, instead of
96 American's stock being held by many individual stockholders, Thames Holdings will
97 acquire American's common stock, and American will become a wholly-owned
98 subsidiary of Thames Holdings which, in turn, is a wholly-owned subsidiary of RWE.

99 **Q. PLEASE DESCRIBE HOW THIS TRANSACTION WILL AFFECT THE DAY-**
100 **TO-DAY OPERATIONS AND MANAGEMENT OF ILLINOIS-AMERICAN.**

101 A. This transaction will not adversely affect the day-to-day operations and management of
102 Illinois-American. RWE/Thames seeks to acquire American in large measure due to
103 American's outstanding reputation for quality management and operation of its
104 subsidiaries, including Illinois-American. Thames is committed to using existing Illinois-
105 American management and expertise. Operational control of Illinois-American will
106 remain as it is today. The transaction will not cause the relocation of the operating
107 headquarters from its current location in Belleville, Illinois. Moreover, it is important to
108 note that, upon closing of the transaction, Thames will expand American's corporate
109 headquarters in Voorhees, New Jersey to manage all of Thames' business operations in
110 North, Central and South America.

Q. IN YOUR OPINION, WILL THE TRANSACTION ADVERSELY AFFECT ILLINOIS-AMERICAN'S ABILITY TO PROVIDE ADEQUATE, RELIABLE, EFFICIENT, SAFE AND LEAST-COST PUBLIC UTILITY SERVICE?

A. No, the transaction will not adversely affect Illinois-American's ability to provide reliable, efficient, safe and least-cost public utility service. Similar to American and Illinois-American, Thames recognizes that customer satisfaction is essential for successful business operations. We share American's commitment to service excellence. In other words, Thames assures this Commission that, following the transaction, Illinois-American will continue to provide high-quality water service that meets or exceeds Illinois regulatory requirements. In addition, we are committed to ensuring that Illinois-American will continue to maintain an adequate level of capital investment and best operating practices to ensure safe and reliable service consistent with applicable requirements.

Q. IS THAMES COMMITTED TO ENSURING THE SECURE OPERATION OF ILLINOIS-AMERICAN'S EXISTING SYSTEMS?

A. We fully recognize and appreciate the increased expectations placed on the United States water industry regarding infrastructure security following the tragic events of September 11. Thames pledges its unqualified commitment to carrying out a comprehensive security plan, not only during the period of transition, but also for the years to come. A renewed emphasis on security is already well underway throughout the American system. While, for obvious reasons, specifics with regard to the companies' security initiatives are highly confidential, the companies are prepared to share their initiatives with

appropriate officials in a manner that will balance the mutual objectives of comprehensive security planning and national security.

Q. PLEASE DESCRIBE THE IMPACT OF THE PROPOSED TRANSACTION ON ILLINOIS-AMERICAN'S EMPLOYEES.

A. Illinois-American's and American's employees are key to providing customers with excellent, reliable service. This quality of service is also a primary focus and priority for Thames, and is one of the reasons the companies are such a compatible combination. The transaction will not result in any change in the existing management and officers of Illinois-American. All collective bargaining agreements will also be honored.

Q. WHAT, IF ANY, IMPACT WILL THE TRANSACTION HAVE ON ILLINOIS-AMERICAN'S RATES?

A. The transaction itself will not result in any increase in rates. Illinois-American will continue to operate under its existing tariffs and rate structures. The transaction is an acquisition of the stock of American. It is anticipated that operations of the subsidiaries of American will not change as a result of the transaction. Relying on current management policies and control over operations, Illinois-American will continue to ensure that its rates are just and reasonable. None of the outstanding debt owed and recorded as liabilities on the books of Illinois-American will be affected by the Agreement, and the transaction will cause no changes in the balance sheet or financial position of Illinois-American.

Further, the transaction will not result in any adverse changes in Illinois-American's policies with respect to financing, accounting, capitalization, rates,

depreciation, maintenance, or other matters affecting the public interest or utility operations.

Illinois-American has reported its existing agreements and transactions with affiliated companies to the Commission. As of the present time, we have identified no transactions in which Illinois-American is acquiring goods or services from, or providing goods or services to, companies that will become affiliates as a result of the transaction contemplated by the Agreement. We fully understand that, should such transactions or arrangements arise, Illinois-American will be required to make all necessary disclosures and/or filings in accordance with the PUA and the Commission's rules. Illinois-American's rates will reflect the costs of such transactions only to the extent permitted by future Commission orders.

Subject to appropriate protection of confidential information, the books and records of RWE and/or Thames will be made available to the Commission to the extent necessary for auditing of costs incurred by either that are allocated to Illinois-American for recovery in rates. Thames also acknowledges the Commission's statutory authority to perform management audits, and will cooperate fully in that regard. Subject again to appropriate confidentiality agreements, Thames will provide copies of Federal Income Tax returns in those cases where Illinois-American income is included in a consolidated return with other subsidiaries of Thames or RWE. Finally, Thames will comply with any Commission requirements to make available personnel who are familiar with the records identified above.

Q. WILL THE TRANSACTION SIGNIFICANTLY IMPAIR ILLINOIS-AMERICAN'S ABILITY TO RAISE CAPITAL ON REASONABLE TERMS AND MAINTAIN A REASONABLE CAPITAL STRUCTURE?

A. No. Although American has been successful in raising capital, the financial resources and backing of RWE/Thames will enhance Illinois-American's and American's access to capital markets.² Access to capital markets at reasonable costs will be a benefit to Illinois-American and its customers. The enhanced access to capital will allow the continued maintenance of a reasonable cost structure.

Q. SECTION 7-204(C) OF THE PUA REQUIRES THE COMMISSION TO RULE ON: (1.) THE ALLOCATION OF ANY SAVINGS RESULTING FROM THE TRANSACTION; AND (2.) WHETHER JOINT APPLICANTS SHOULD BE ALLOWED TO RECOVER THE COSTS INCURRED TO ACCOMPLISH THE TRANSACTION. WOULD YOU PLEASE COMMENT ON THIS REQUIREMENT?

A. Thames does not seek recovery of any acquisition premium or costs to accomplish the proposed transaction, and Thames does not intend to pass such costs through to Illinois-American. Therefore, under Section 7-204(c), the Commission should rule that no costs incurred in accomplishing the transaction are recoverable in rates. Moreover, since Thames does not currently maintain operations in Illinois, Thames does not expect synergy savings to result in Illinois from the proposed transaction. Accordingly, under Section 7-204(c), the Commission should rule that savings reflected in future rate case test years, if any, should be allocated in full to customers.

² A copy of RWE and Thames' credit ratings is included in the Appendix to Testimony as Exhibit K.

198 **Q. CAN YOU PROVIDE SOME EXAMPLES OF THE BENEFITS THAT CAN BE**
199 **EXPECTED AS A RESULT OF THIS TRANSACTION?**

200 A. Yes. Thames and Illinois-American can be expected to benefit from combination of the
201 best practices of both American's and Thames' systems. In terms of customer support
202 and service, we anticipate that Illinois-American customers will benefit in those instances
203 where this partnership delivers the economies and efficiencies that are inherent when two
204 industry leaders share their practical knowledge and experience. The benefits that we
205 expect will be realized by Illinois-American and its customers include the following:

206 **Security**

207 Since the tragic events of September 11, a renewed emphasis on security has been
208 underway throughout the American water system. American has been reviewing the
209 security measures in place throughout its system. As a result of this review, Illinois-
210 American is evaluating and implementing new methods and procedures to better ensure
211 the security of its operations. Thames, with water operations around the globe, has
212 considerable experience in operating water facilities and systems in regions where
213 security concerns have been a fact of life for some time. For example, Great Britain has
214 been subject to threat by IRA factions for decades, and by Middle Eastern terrorists since
215 the Gulf War. Thames stands ready and willing to utilize its expertise to enhance Illinois-
216 American's security efforts. Although we will remain separate independent companies
217 until the transaction closes, we look forward to beginning the exchange of best practices
218 as soon as possible. One important area for such an exchange may be within the scope of
219 facility security, a topic that has come to the fore in the aftermath of September 11. We
220 firmly believe that Illinois-American -- and ultimately its customers -- will benefit

significantly from sharing Thames' extensive experience in developing and implementing comprehensive security measures to protect its customers and employees throughout the world. Thames pledges its unqualified commitment to implement and maintain a comprehensive security plan, not only during the period of transition, but also for the years to come.

Environmental Matters

Further, both companies recognize the importance of conducting their operations in an environmentally compatible manner and, as such, actively promote nature conservation on their sites. American and its subsidiaries have a strong environmental track record that will be further enhanced through its association with Thames. American consistently achieves outstanding records of annual compliance with Federal and State Regulations. American's subsidiaries have received 47 awards from the U.S. Environmental Protection Agency Partnership for Safe Water. Thames is also strongly committed to environmental protection, and numerous Thames Water sites have been awarded the internationally recognized ISO 14001 Environmental Standard. Thames also works with and supports a wide range of environmental and conservation groups internationally, in part by voluntarily conducting surveys to assist these groups in implementing biodiversity protection projects. Additionally, Thames utilizes "green energy," with seventeen combined heat and power plants running bio-gas and two sludge-powered generators. The transaction will enable American and Thames to join together to continue to enhance environmentally-friendly service for their customers.

Service Standards

In the area of service standards, American Water has earned an enviable reputation throughout the United States. It maintains its facilities in superior condition, and ensures safe, reliable and high-quality service to its customers through capital investment in its infrastructure. Similarly, Thames is committed to excellence in its water quality and service standards throughout the world. In fact, the Thames track record of compliance with drinking water standards in the UK is now 99.89%, while wastewater effluent compliance is 99.99%. Since privatization in 1989, Thames has invested in excess of \$6 billion in enhancing the quality of its service, including construction of an advanced water treatment system and major renovations of water mains and sewage treatment works. Throughout its system, Thames has established numerous programs to improve the quality of its service, including cost-optimized network renewal and refurbishment and the development of ultra-violet disinfection of drinking water. Thames has every intention of continuing the long and proud service that has come to be expected of the American Water System generally, and Illinois-Water in particular.

Customer Service

For many years, both companies have demonstrated their strong commitment to customer service and responsiveness. Illinois-American is dedicated to providing its customers with continuous customer service. Its parent corporation, American, recently opened a state-of-the-art Customer Service Center located in Alton, Illinois to assist its customers 24 hours a day. Likewise, Thames has a 24-hour customer service center that has won the UK Utility Industry Achievement Award for Excellence three years in a row. One of the key customer service issues facing the utility industry is integration between the call

center and the field service function. Thames has developed and implemented an integrated approach to service management inquiries by installing the latest information technology for mobile field applications. This provides a direct, real-time link between the system in use in the Call Center and the technicians in the field. This real-time connection delivers critical Geographic Information Systems work management system data. The customer benefits by having problems ascertained, analyzed, and addressed by field personnel in a very accurate and efficient manner. The new system results in a much more professional and problem-free service, and reduces the need for customers to make repeated calls to different parts of the organization. American will take advantage of Thames' experience to implement a similar service, thereby further improving service and reducing the time and cost of delivery. Together, these quality organizations will continue their commitment and improve customer service by utilizing the best practices of both organizations.

Research and Development

In the area of research and development, American and Thames are both recognized industry leaders. The pooling of our collective expertise will make the combined entity a world leader in this area. Notably, Thames has an annual research and development budget of \$13 million. Thames has developed cutting-edge technologies in the areas of transmission and distribution.

Community Service

The transaction will positively impact community development in the areas served by Illinois-American. Thames, RWE, and American all share a long history of service in the communities where they operate. For American, financial contributions to the

community are generally focused on environmental programs, as well as on initiatives that support the next generation of community leaders. American's involvement goes far beyond financial support, as it routinely involves the personal participation and leadership of employees in important community programs. Thames also has a long and illustrious track record of investing in local communities, particularly in support of the environment and extra-need customers. For example, Thames supports its employees' involvement in community groups through a payroll program called "Give as You Earn." In this program, Thames matches charitable contributions raised by teams of employees. Additionally, RWE participates in numerous community-oriented projects around the globe. It sponsors a variety of projects in areas ranging from promoting arts and culture, to programs modernizing the water infrastructure in developing countries. Companies such as American, RWE, and Thames understand that a good reputation must be earned. They also understand that it takes a great deal of work and commitment to maintain such reputations. Clearly, the philosophy of corporate responsibility resides at the core of the RWE, Thames and American cultures, and the philosophy will continue.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes. Thames, the entity responsible for RWE's water operations, looks forward to the continued operation, maintenance and growth of Illinois-American, which has provided quality service to Illinois customers for more than 100 years.

CURRICULUM VITAE

Name: Michael Carmedy

Date of Birth: 5 June 1964

Education: 1983-86 University of Kent, Canterbury
Qualifications Awards:
BA (Hons) Accountancy, 2:1
Winner of the Arthur Andersen Tax Prize 1985

1975-82 St Johns Comprehensive School, Co. Durham
Qualifications:
Gained 3 x 'A' Levels (English, Geography, Economics)
Gained 9 x 'O' Levels

Professional Qualification: Chartered Accountant (ACA) - Qualified 1990

Work Experience:

August 2001 to date

Senior Vice-President and Commercial Director, Thames Water Americas

Primary duties:

- Manage the regulatory approval of American Water Works.
- Commercial lead with regard to Thames Water Americas project bids.
- Risk management.

January 2000 to 31 July 2001 (full-time from 1 October 2000)

Vice-President and Commercial Director, Thames Water North America (TWNA)

Primary duties:

- Provide guidance and support as required to the E'town management team, ensuring a common understanding of business priorities.
- Management of the integration process between Thames Water and Elizabethtown.
- Commercial lead with regard to TWNA project bids.
- Project Manager for all TWNA acquisition activities.

April 1998 to October 2000

Financial Controller, TWUL Engineering and Acquisition Manager for TW Plc.

Financial Controller responsibilities include:

- Primary responsibility for all financial matters within Engineering, reporting to the Engineering Director.
- Managing the preparation of business plans, budgets and re-forecasts.
- Financial/Commercial advice regarding all key business issues.
- Establishment and management of a credible finance team.

Acquisition Manager responsibilities include:

- Project management of major acquisition bids, reporting to the Finance Director, TW Plc.
- Management of due diligence efforts.
- Management and co-ordination of external advisers.

April 1991 to March 1998

Various roles within the Thames Water Plc Internal Audit Department, joining as a Senior Auditor, being promoted to Supervising Auditor and in September 1996 to Investigations and Special Audits Manager

Key responsibilities included:

- Project management of major corporate finance activities, including the disposal of two major subsidiaries following Thames' focus on core operating activities.
- Establishment of audit methodologies for large build/own/operate/transfer (BOOT) and concession type contracts.
- Business reviews of International subsidiaries, including companies in the US, Thailand, Hong Kong, Singapore and Australia.
- Management of Internal Audit's reviews of non-TWUL subsidiaries.
- Management and performance of operational audit reviews.
- Establishment and management of Internal Audit's performance of US subsidiary year end financial audits.

May 1990 to March 1991

Moore Rowland, Chartered Accountants, Audit Senior

- Performance and management of financial audits.
- Primary responsibility for first audit of new clients.

August 1986 to April 1990

Fraser and Russell, Chartered Accountants, Audit Trainee